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Alternative Tax Strategies for Local Governments

Abstract

During the fiscal year 2004-05, New Yorker's paid approximately \$111 billion in state and local taxes. Of this total, local taxes accounted for 55% or \$61 billion. Local tax revenues come mainly from the property tax and sales tax, which account for \$34 billion and \$10 billion, respectively. Taxes are important to development for two reasons. First, the tax burden on low and middle class families affects local citizen's standard of life, access to affordable housing, and level of expendable income. Second, states and municipalities have long relied on lowering taxes and providing tax incentives as their primary tools for attracting business. Traditional tax strategies must be re-examined because of problems in both areas.

Keywords

Buffalo, Government, Taxation, Fact Sheet, PPG, PDF

ALTERNATIVE TAX STRATEGIES FOR LOCAL GOVERNMENTS

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How do local governments generate revenue?

During the fiscal year 2004-05, New Yorker's paid approximately \$111 billion in state and local taxes. Of this total, local taxes accounted for 55% or \$61 billion. Local tax revenues come mainly from the property tax and sales tax, which account for \$34 billion and \$10 billion, respectively.¹

Why are tax strategies important to community and economic development?

Taxes are important to development for two reasons. First, the tax burden on low and middle class families affects local citizens standard of life, access to affordable housing, and level of expendable income. Second, states and municipalities have long relied on lowering taxes and providing tax incentives as their primary tools for attracting business. Traditional tax strategies must be re-examined because of problems in both areas.

What do existing tax structures mean for the current tax burden in New York State?

New York State's average tax burden has reached its highest level on record and among the 50 states is exceeded only by Connecticut, a state that does not suffer from the same level of poverty as New York.² New York's total tax burden is computed by adding the averages of state and local taxes (13.8 percent of personal income) with the average total of federal taxes (23.3 percent of personal income). New York's total tax burden, which on average amounts to 37.1% of a citizen's personal income, is well above the national average of 32.7%.³ This gap between New York and the national average has consistently grown since 1970, when the gap was only 2.8 percentage points. In addition, the average of New York's state and local taxes is among the highest in the nation. In 2005, this average trailed only Maine.⁴ New York's growing tax burden can be blamed on many factors and one such

Upstate counties leading the nation
If you own a home in these Upstate New York counties you're paying some of the highest property taxes in the United States — compared to the value of your home.

County	Average property taxes	Average home value	Taxes as % of home value	National rank*
Wayne County	\$2,912	\$99,200	2.9%	1
Niagara County	\$2,638	\$90,700	2.9%	2
Monroe County	\$3,407	\$120,400	2.8%	3
Erie County	\$2,768	\$108,900	2.5%	4
Chautauqua County	\$1,899	\$75,300	2.5%	6
Onondaga County	\$2,896	\$115,900	2.5%	7
Cayuga County	\$2,256	\$93,200	2.4%	8
Chemung County	\$1,840	\$76,400	2.4%	9
Schenectady County	\$3,471	\$145,300	2.4%	10
Steuben County	\$1,955	\$82,100	2.4%	11
Oneida County	\$2,165	\$91,300	2.4%	12
Ontario County	\$2,690	\$114,000	2.4%	14
Oswego County	\$1,901	\$81,900	2.3%	16
Cattaraugus County	\$1,719	\$74,100	2.3%	17
Broome County	\$2,094	\$93,400	2.2%	22
Tompkins County	\$3,234	\$146,500	2.2%	25
Madison County	\$2,230	\$103,200	2.2%	31
U.S. average			0.9%	

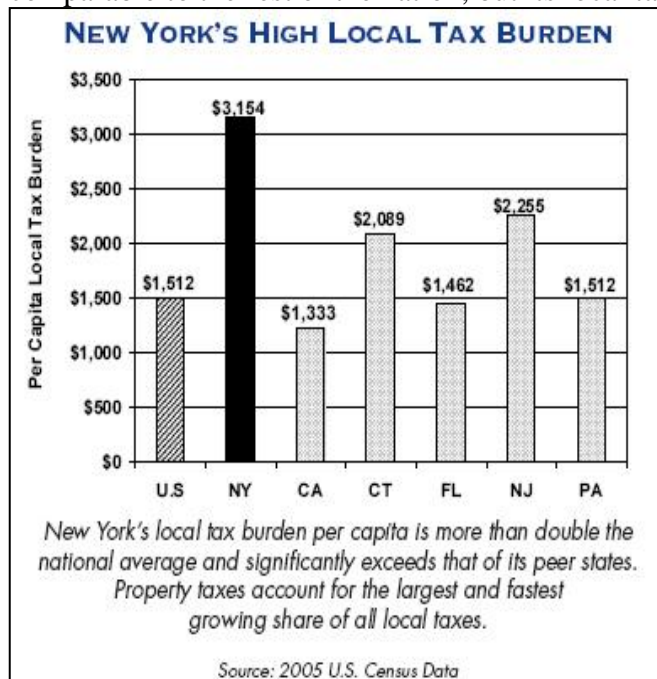
* Ranked out of 783 counties nationwide
Source: American Community Survey (Census Bureau) and the Tax Foundation, 2006. The Post-Standard

factor is the significant property tax levied on New York homeowners. In 2006, 17 upstate New York counties registered among the highest 31 counties nationwide for taxes as a percentage of home value (see figure left).⁵

The growing tax burden in New York State is increasingly being felt by the middle and lower class. Since the 1970's, New York State's personal income tax has undergone significant restructuring. In 1972, New York State had 14 different tax brackets for personal income. These brackets ranged from 2% to 15% based on total income. The state has eliminated most of its brackets and now has only five, all of which are between 4% and 6.85% of personal income. The result is that high-income citizens' tax rates have decreased while low-income citizens' rates have increased.⁶

How can state and local leaders reduce the tax burden for lower and middle-class citizens?

To reduce the tax burden for New York residents, lawmakers must focus on local taxes. According to a report produced by the Spitzer administration, New York's state taxes are comparable to the rest of the nation, but its local taxes are by far the highest (see "New



York's High Local Tax Burden).⁷

To reduce local tax burdens, former Governor Spitzer enacted a comprehensive program to provide increased aid to distressed municipalities and increases in property tax relief. Spitzer's program involved:

- Billions in property tax relief through the School Tax Relief (STAR) program which targeted more than \$1 billion to middle income homeowners.
- Restructuring the Aid and Incentives for Municipalities (AIM) program to commit more cash to distressed municipalities.
- Creation of the Commission on Local Government Efficiency and Competitiveness to promote local government consolidation and sharing of regional services. The aim of the Commission is to identify new ways for municipalities to decrease costs and save taxpayer dollars.
- Significant increases in school aid so that local municipalities will have decreased school expenditures.

Spitzer's plan to decrease the local tax burden was essentially two-fold: provide funding to local municipalities to reduce their spending and examine local government spending programs to identify and fix inefficiencies.⁸ This plan involves increased state spending, and because of the current fiscal crisis, Governor David Patterson has sought ways to

decrease the local tax burden without increased state spending. Patterson has proposed a tax cap for school districts outside of New York's five largest cities.⁹ The goal of this cap would be to curb constantly increasing local tax burdens throughout the state.

Can local governments look to other sources for tax revenues?

Rather than focusing on the reduction of municipal spending, many local governments throughout the country have focused their tax reforms on the development of new sources of revenue. Two new tax policies being considered at the federal and state levels are eco-taxation and cyber-taxation.

- *Eco-taxation:* The driving focus of eco-taxation is to collect revenue through environmental and land-based taxes rather than income, capital, and consumption of necessities. Advocates argue that eco-taxes have many advantages over traditional taxation, including that they are cheaper to collect, fall clearly and directly on the ultimate payer, embody no favoritism or exceptions, correspond to the payer's ability to pay, and do not bring about undesirable economic distortions.¹⁰
- *City Income Taxes:* In 1939, Philadelphia became the first American city to levy a city income tax. Following Philadelphia's lead, many other cities introduced similar taxes throughout the Midwest, and most frequently in Ohio and Pennsylvania. By 1967, over 170 municipalities had levied city income taxes.¹¹ New York is one city that imposes a personal income tax on its residents. In New York City, every income-earning resident is subject to the tax that is based on the New York State personal income tax. To determine the tax, a resident uses the same filing status and taxable income as for State purposes, but different tax rates and credits are applied.¹²
- *Real Estate Transfer Tax:* Many states and municipalities have opted to collect real estate transfer taxes. RETTs are collected at the transfer of residential properties, vacant land, industrial properties, commercial properties, or retail properties. A RETT is usually a rate applied to the sales price of the property, but it can also be levied as a set dollar amount per \$1,000 of value of a property sold.¹³



What are some examples of alternative local taxes being implemented throughout the United States?

Several major municipalities across the United States have devised alternative taxes in order to take the strain of income, sales and property taxes off of citizens. Most of these alternative taxes were created with environmental concerns in mind, and the use of eco-taxes is becoming more and more prevalent. Examples of eco-taxes include:

- *Carbon Tax:* A carbon tax is a tax on the carbon content of fossil fuels. Beyond being an alternative way of raising revenue, carbon taxes are meant to convey price signals and spur carbon-reducing investment and low-carbon behavior.¹⁴

Currently, Boulder, CO and San Francisco, CA are the only US cities that levy a carbon tax. Boulder's carbon tax costs the average household \$1.33 per month and is expected to raise about \$1 million annually.¹⁵ San Francisco's carbon tax is the nation's first carbon tax on businesses. The tax, approved in May 2008, will require businesses to pay 4.4 cents per ton of carbon dioxide emitted.¹⁶ Carbon taxes have also been implemented in Canadian provinces (Quebec, British Columbia), New Zealand, Great Britain, Sweden, and Finland.

- *Bottled Water Tax:* To offset the negative environmental impact of disposable plastic water bottles, the city of Chicago has levied a bottled water tax. The tax, which will take effect on January 1, charges five cents per bottle, and the city expects that it will raise \$10.5 million annually.¹⁷



- *Plastic Bag Tax:* Like the bottled water tax, this tax is meant to diminish the negative environmental impact of wasted plastic products. Recently, Mayor Greg Nickels of Seattle, WA proposed a 20-cent tax on disposable plastic bags. The tax, which still requires approval from the city council, would take effect on January 1, 2009.¹⁸ Following the lead of Seattle and many European countries, New York's Mayor Michael Bloomberg has proposed a six-cent charge for every plastic bag used by shoppers. New York City officials estimate that the tax, which is being marketed as a fee, could generate \$16 million per year. The reason that Bloomberg has proposed the charge as a fee is so that he can circumvent the state legislative approval process, which is necessary for all taxes. Similar measures are being considered in other US municipalities including Los Angeles and Dallas.¹⁹



- *Cigarette Tax:* Focused on public health, cigarette taxes have long been levied at the state, and city level. In New York City, the combined state and city taxes amount to \$4.25 per pack.²⁰ In Ohio, Cuyahoga County, home to Cleveland, levies a 3-cent charge on each cigarette and dedicates the proceeds to supporting arts and cultural organizations.²¹

How are existing tax structures used in economic development?

Local and state officials have long focused on creating jobs and growing the economy when dealing with economic development initiatives. Their main tool has been to offer tax cuts and incentives to lure businesses to their municipalities. Unfortunately, tax cuts and incentives have become increasingly criticized for their inability to produce significant returns on money invested. Research on incentive based economic development has shown that most businesses fail to create as many jobs as promised. In New York State, a lack of accountability has allowed under performing businesses to continue receiving aid. In addition, political abuses and irresponsibility has allowed otherwise ineligible communities and businesses to secure incentives that would produce better results if they were spent in more needy areas.

What, other than tax breaks and incentives, can local governments use to promote economic development?

Alternative economic development strategies have gained increasing popularity because of the shortcomings of tax breaks and incentive based strategies. Researches have suggested that rather than providing breaks from taxes, the taxes should be reinvested into communities that need development assistance. Reinvestment of tax revenues may stimulate economic growth and result in the creation of more jobs than traditional incentive programs.²²

The idea behind this approach is that businesses will be more attracted to, will benefit more from, and will stay longer in communities that can provide a beneficial environment that is rich in resources necessary for successful business. To provide this environment, governments should invest in infrastructure, workforce development, and quality of life.²³ Rather than slashing taxes in competition with other municipalities for business, local



governments should focus on highlighting their strengths and re-investing tax revenues to improve their appeal to businesses. To do this, local governments should identify key characteristics of their local economy, and design strategies to enhance local competitiveness and support local industries. Rather than focusing on new businesses, local governments should work with existing firms to enhance business retention and job growth through expansion. In addition, tax revenues should be focused on community

development. Businesses are attracted to communities that exhibit a high quality of life and have a supply of well-trained workers. Local governments should invest in low-income neighborhoods through community development loan funds, community development corporations, welfare to work programs, micro-enterprise programs, and vocational training programs. Finally, local governments must develop a working relationship with the non-profit sector. Non-profits can provide social support, training, community organizing, and economic development expertise.²⁴

¹ <http://www.cbcny.org/CBC%20%20Local%20Taxes%20in%20NY%20%20FINAL1.pdf>, Page 4

² <http://albanysinsanity.wnymedia.net/blogs/2007/05/22/total-ny-tax-burden-at-record-level/>, <http://www.empirecenter.org/2007/05/totalnytaxes.cfm>

³ <http://albanysinsanity.wnymedia.net/blogs/2007/05/22/total-ny-tax-burden-at-record-level/>, <http://www.empirecenter.org/2007/05/totalnytaxes.cfm>

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- ⁴ <http://money.cnn.com/pf/features/lists/taxesbystate2005/>
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- ⁹ http://findarticles.com/p/articles/mi_qn4180/is_20080605/ai_n25503664
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- ²¹ http://www.cleveland.com/entertainment/index.ssf/2008/04/cuyahoga_county_cigarette_tax.html
- ²² <http://www.fiscalpolicy.org/lynch.html>
- ²³ http://www.cdtoolbox.net/economic_development/000200.html
- ²⁴ http://www.cdtoolbox.net/economic_development/000200.html